CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

June 9, 2006

S. 2766

National Defense Authorization Act for Fiscal Year 2007

As reported by the Senate Committee on Armed Services on May 9, 2006

SUMMARY

S. 2766 would authorize appropriations totaling $509 billion for fiscal year 2007 for the military functions of the Department of Defense (DoD), for activities of the Department of Energy (DOE), and for other purposes. That total includes $50 billion for military operations in Iraq and Afghanistan. The bill also would authorize an estimated $68 billion in supplemental appropriations for 2006, primarily for the costs of those operations not covered by appropriations provided earlier in the year. (A supplemental appropriations act to provide that amount has been passed by the Senate, but as of this date, that legislation has not yet been enacted into law.)

In addition, S. 2766 would prescribe personnel strengths for each active-duty and selected reserve component of the U.S. armed forces. CBO estimates that appropriation of the authorized amounts would result in additional outlays of $572 billion over the 2006-2011 period. Including outlays from funds previously appropriated, spending for defense programs authorized by the bill would total about $530 billion in 2007, CBO estimates. (By comparison, CBO estimates that such spending will total about $518 billion in 2006, assuming appropriation of pending supplemental appropriations.)

The bill also contains provisions that would both increase and decrease costs of discretionary defense programs over the 2008-2011 period. Most of those provisions would affect DoD force structure or would provide added compensation, benefits, or health care coverage to members of the armed forces. Provisions affecting force structure would lower costs by several billion dollars annually beginning in 2008. Certain other provisions—primarily those related to compensation and health care benefits—would increase costs between $1 billion and $2 billion annually.

The bill contains provisions that would both increase and decrease direct spending, primarily by expanding DoD's ability to use third-party financing for the construction of military housing and through changes to survivor benefits and TRICARE. We estimate that those provisions combined would increase direct spending by $1.4 billion over the 2007-2011 period and by $2.0 billion over the 2007-2016 period. In addition, enacting the bill would decrease federal revenues by an estimated $1 million over the 2007-2016 period.

Section 4 of the Unfunded Mandates Reform Act (UMRA) excludes from the application of that act any legislative provisions that enforce the constitutional rights of individuals. CBO has determined that section 1042 would fall within that exclusion because it would expand the authority of the President to employ the armed service to protect individuals' civil rights. Therefore, CBO has not reviewed that section of the bill for mandates.

Other sections of S. 2766 contain both intergovernmental and private-sector mandates as defined in UMRA. It would prohibit employers and other providers of group health coverage from offering incentives to military retirees and their dependents to decline enrollment in the group health plan in favor of relying on DoD's TRICARE health program as the primary source of health coverage. CBO estimates that the costs of that mandate for state and local governments would likely fall below the threshold for intergovernmental mandates ($64 million for intergovernmental mandates in 2006, adjusted annually for inflation), but that the costs to private employers would likely exceed the threshold for private-sector mandates ($128 million in 2006, adjusted annually for inflation).

This bill contains several provisions that would benefit state and local governments. Some of those provisions would authorize aid for certain local schools with dependents of defense personnel and convey of certain parcels of land to state and local governments. Any costs to those governments would be incurred voluntarily as a condition of receiving federal assistance.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 2766 is summarized in Table 1. Most of the costs of this legislation fall within budget function 050 (national defense).

BASIS OF ESTIMATE

For this estimate, CBO assumes that S. 2766 will be enacted near the start of fiscal year 2007 and that the authorized amounts for 2006 and 2007 will be appropriated.

TABLE 1. BUDGETARY IMPACT OF S. 2766, THE NATIONAL DEFENSE AUTHORIZATION ACT FOR FISCAL YEAR 2007 (by fiscal year, in millions of dollars)

	2006	2007	2008	2009	2010	2011
SPENDING SUBJECT TO APPROPRIATION						
Spending Under Current Law for Programs Authorized by S. 2766						
Budget Authority [a]	482,814	0	0	0	0	0
Estimated Outlays	496,018	163,450	51,119	19,003	8,169	3,654
Proposed Changes						
Authorization of Supplemental Appropriations for 2006						
Estimated Authorization Level [b]	67,706	0	0	0	0	0
Estimated Outlays	21,555	29,193	11,839	3,178	1,036	442
Authorization of Regular Appropriations for 2007						
Authorization Level	0	459,185	0	0	0	0
Estimated Outlays	0	301,956	107,753	31,036	10,017	3,833
Authorization of Appropriations for 2007 for Military Operations in Iraq and Afghanistan						
Authorization Level [b]	0	50,000	0	0	0	0
Estimated Outlays	0	35,708	10,526	2,475	721	239
Spending Under S. 2766						
Estimated Authorization Levels	550,520	509,185	0	0	0	0
Estimated Outlays	517,573	530,307	181,237	55,692	19,943	8,168
CHANGES IN DIRECT SPENDING						
Estimated Budget Authority	0	458	493	318	122	117
Estimated Outlays	0	307	390	239	262	218
CHANGES IN REVENUES						
Thrift Savings Program						
Estimated Revenues	0	*	*	*	*	*

NOTES: For 2007, the authorization levels under "Proposed Changes" include amounts specifically authorized by the bill. The bill also implicitly authorizes programs in 2008 through 2011; those authorizations are not included above (but are shown in Table 3) because funding for those programs would be covered by specific authorizations in future years.

* = Reduction in revenues of less than $500,000.

a. The 2006 level is the amount appropriated for programs authorized by the bill. That amount is slightly lower than the comparable figure presented in CBO's cost estimate for H.R. 5122, the National Defense Authorization Act for Fiscal Year 2007, as reported by the House Committee on Armed Services on May 5, 2006, because H.R. 5122 would authorize appropriations for some existing programs that would not be authorized by S. 2766.

b. These authorizations are primarily for costs associated with operations in Iraq and Afghanistan. For 2006, section 1002 of the bill would adjust existing authorizations to reflect added funding provided in supplemental appropriations; the amount shown above is equal to appropriations that would be provided to DoD by H.R. 4939, the Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery, 2006, as passed by the Senate. For 2007, title XIV of the bill would authorize specific amounts of funding for DoD; the amount shown above is the sum of the stated authorizations that would be provided by that title.

Spending Subject to Appropriation

The bill would specifically authorize appropriations totaling $509 billion in 2007 (see Table 2). Nearly all of that amount falls within budget function 050 (national defense), while a small portion—$55 million for the Armed Forces Retirement Home—falls in budget function 600 (income security).

For 2006, the bill also would adjust existing authorizations to reflect final Congressional action on pending supplemental appropriations for defense activities, primarily in Iraq and Afghanistan. For this estimate, CBO assumes those appropriations to DoD will be provided by early July of 2006 and will total $68 billion, the amount approved by the Senate. If enacted, that funding would be in addition to the $50 billion already provided for those operations for 2006.

Although most of the $509 billion in funding for 2007 authorized by the bill would be for full-year costs of defense programs, $50 billion of that amount would be for DoD costs associated with continuing operations in Iraq and Afghanistan. That amount would likely cover only a portion of 2007 costs associated with those operations.

The estimate assumes that the amounts authorized for 2007 will be appropriated near the start of fiscal year 2007. The estimated outlays from authorizations of regular appropriations are based on historical spending patterns. Estimated outlays from the $50 billion that the bill would authorize for operations in Iraq and Afghanistan would primarily result from obligations incurred during the first part of the year.

The bill also contains provisions that would both increase and decrease various costs, mostly for changes in endstrength, military compensation, and health benefits, that would be covered by the fiscal year 2007 authorization and by authorizations in future years. Table 3 contains estimates of those amounts.

Force Structure. The bill would affect force structure primarily by setting endstrength levels for the armed forces.

Military Endstrength. Title IV would authorize active and reserve endstrength levels for 2007 and would repeal current minimum endstrength requirements for active-duty personnel.

The bill would specifically authorize regular appropriations of $112 billion and additional appropriations for operations in Iraq and Afghanistan of $7.3 billion for costs of military pay and allowances in 2007.

TABLE 2. SPECIFIED AUTHORIZATIONS IN S. 2766

Category	By Fiscal Year, in Millions of Dollars 2007	2008	2009	2010	2011
Authorization of Regular Appropriations					
Department of Defense					
Military Personnel [a]					
Authorization Level	112,043	0	0	0	0
Estimated Outlays	106,775	4,594	224	112	0
Operation and Maintenance					
Estimated Authorization Level [b]	151,273	0	0	0	0
Estimated Outlays	111,150	32,312	4,693	1,561	679
Procurement					
Estimated Authorization Level [b]	86,688	0	0	0	0
Estimated Outlays	27,783	33,195	16,206	4,896	2,143
Research and Development					
Estimated Authorization Level [b]	73,847	0	0	0	0
Estimated Outlays	40,403	27,542	4,166	1,037	294
Military Construction and Family Housing					
Authorization Level	17,098	0	0	0	0
Estimated Outlays	2,512	5,702	5,052	2,499	767
Revolving and Management					
Authorization Level	2,436	0	0	0	0
Estimated Outlays	1,760	442	115	72	30
General Transfer Authority					
Authorization Level	0	0	0	0	0
Estimated Outlays	800	-160	-320	-160	-80
Subtotal, Department of Defense					
Authorization Level	443,385	0	0	0	0
Estimated Outlays	291,183	103,627	30,136	10,017	3,833
Atomic Energy Defense Activities [c]					
Authorization Level	15,744	0	0	0	0
Estimated Outlays	10,725	4,118	900	0	0
Other Programs					
Authorization Level [d]	56	0	0	0	0
Estimated Outlays	48	8	0	0	0
Subtotal, Authorization of Regular Appropriations					
Authorization Level	459,185	0	0	0	0
Estimated Outlays	301,956	107,753	31,036	10,017	3,833

(Continued)

TABLE 2. CONTINUED

Category	By Fiscal Year, in Millions of Dollars 2007	2008	2009	2010	2011
Authorization of Appropriations for Military Operations in Iraq and Afghanistan					
Military Personnel					
Authorization Level	7,336	0	0	0	0
Estimated Outlays	7,314	0	0	0	0
Operation and Maintenance					
Authorization Level	37,537	0	0	0	0
Estimated Outlays	25,764	8,895	1,828	589	218
Procurement					
Authorization Level	2,127	0	0	0	0
Estimated Outlays	442	967	527	110	31
Classified Activities					
Authorization Level	3,000	0	0	0	0
Estimated Outlays	2,013	702	195	60	15
Transfer Authority					
Authorization Level	0	0	0	0	0
Estimated Outlays	175	-38	-75	-38	-25
Subtotal, Iraq and Afghanistan					
Authorization Level	50,000	0	0	0	0
Estimated Outlays	35,708	10,526	2,475	721	239
Total Specified Authorizations					
Authorization Level	509,185	0	0	0	0
Estimated Outlays	337,664	118,279	33,511	10,738	4,072

a. For purposes of this estimate, CBO assumes that the authorization of appropriations in section 421 for military personnel includes $11,158 million for accrual payments for the TRICARE For Life program.

b. These authorization levels include the estimated effects of an undistributed reduction of $951 million from amounts that would be authorized in titles I, II, and III of the bill.

c. These authorizations are primarily for atomic energy activities within the Department of Energy.

d. This authorization includes $54.8 million for the Armed Forces Retirement Home and $1.5 million for the National Foreign Language Coordination Council.

TABLE 3. ESTIMATED AUTHORIZATIONS OF APPROPRIATIONS FOR SELECTED PROVISIONS IN S. 2766

Category	By Fiscal Year, in Millions of Dollars 2007	2008	2009	2010	2011
FORCE STRUCTURE					
Navy and Air Force Active-Duty Endstrengths	-2,324	-4,783	-4,925	-5,068	-5,218
Army and Marine Corps Active-Duty Endstrengths	39	81	83	86	88
Reserve Component Endstrengths	-105	-216	-223	-231	-238
Reserve Technicians	49	102	106	109	113
COMPENSATION AND BENEFITS					
Pay Raises	196	401	414	428	442
Expiring Bonuses and Allowances	1,527	793	303	287	199
Special Pay for Reserve Health Care Professionals	10	12	12	2	0
Accession Bonuses for Health Specialties	19	5	0	0	0
Voluntary Separation Pay	132	311	514	518	496
Health Professions Scholarships and Financial Assistance	91	93	96	100	103
Loan Repayment for Health Professionals	4	8	12	13	13
Survivor Benefit Plan	23	23	23	24	24
Other Provisions	14	4	2	2	2
DEFENSE HEALTH PROGRAM					
TRICARE Use by Employed Retirees	0	-119	-176	-193	-212
TRICARE Pharmacy Program	49	98	105	104	103
TRICARE Disease Management Programs	10	33	58	79	70
TRICARE Standard Enrollment Fee	20	18	1	1	1
TRICARE Incentive Pay	0	5	8	8	9
OTHER PROVISIONS					
Telecommunications Benefit Program	64	48	39	20	20
Defense Acquisition Challenge Program	0	30	31	32	32
Matters Relating to Other Nations	45	45	5	5	5

NOTES: For every item in this table, the 2007 levels are included in Table 2 within the totals specifically authorized to be appropriated in the bill. Amounts shown in this table for 2008 through 2011 are not included in Table 1.

Numbers in the text may differ from figures shown here because of rounding.

Under title IV, the authorized endstrengths in 2007 for active-duty personnel and personnel in the selected reserves would total about 1,370,000 and 840,000, respectively. Of those selected reservists, about 74,000 would serve on active duty in support of the reserves. In total, active-duty endstrength would drop by over 34,000 and selected reserve endstrength would decrease by almost 6,000 when compared to levels authorized in 2006.

Section 401 would decrease the Navy's active-duty endstrength by 12,000 and decrease the Air Force's active-duty endstrength by 23,200. CBO estimates that the decrease in endstrength for the Navy and the Air Force combined would cut costs for salaries and other expenses by $2.3 billion in the first year and about $5 billion annually in subsequent years. Section 401 also would increase the active-duty endstrength of the Marine Corps relative to current law amounts by 1,000, which CBO estimates would increase costs by $39 million in the first year and about $80 million per year thereafter. CBO does not ascribe any costs or savings to the endstrength that the bill would specify for active-duty personnel in the Army because it is the same as the endstrength specified for the Army under current law.

Section 402 would repeal the requirement that the armed forces maintain at least the minimum active-duty endstrength levels necessary to support two major regional contingencies. Currently, only the Navy and Air Force are planning to reduce endstrength below the minimum levels set in current law. Over the next five years, the Navy and Air Force have indicated their intention to reduce their combined force levels by over 50,000 personnel. However, because endstrength levels are reviewed by the Administration and the Congress on an annual basis, CBO does not estimate any additional savings due to the repeal of this requirement beyond those already discussed above for section 401.

Sections 411 and 412 would authorize the endstrengths for the reserve components, including those who serve on active duty in support of the reserves. Under this bill, the endstrength for the selected reserve would be reduced by 5,700, mostly in the Army and Navy Reserve, and the endstrength for reservists who serve on active duty in support of the reserves would decrease by over 100. CBO estimates that implementing these provisions would decrease costs for salaries and other expenses for selected reservists by $105 million in 2007 and over $200 million annually in subsequent years compared to the authorized endstrength levels for 2006.

Sections 413 and 414 would authorize the minimum endstrength level for military technicians, who are federal civilian personnel required to maintain membership in a selected reserve component as a condition of their employment. Because those personnel count against overall reserve component endstrengths, their associated drill pay and other military training expenses are already included in CBO's estimate of section 411. However, the reserve components would incur additional costs to maintain these personnel on their civilian support payrolls for periods when they are not training or on active duty. Under this bill, the selected reserve would increase their number of technicians by about 1,300 above currently authorized levels. CBO estimates the increase in civilian salaries and expenses due to the additional personnel would be about $50 million in 2007 and about $100 million annually in subsequent years compared to minimum endstrength levels for technicians in 2006.

Coast Guard Reserve Endstrength. The bill would also authorize an endstrength of 10,000 servicemembers in 2007 for the Coast Guard Reserve. Because this authorization is the same as that under current law, CBO does not estimate any additional costs for this provision.

Aircraft Carrier Force Structure. Section 1011 would repeal the requirement that the Navy maintain 12 operational aircraft carriers. Based on information provided by the Navy, CBO assumes that the U.S.S. John F. Kennedy (CV-67) would be retired immediately. Built in the 1960s, the U.S.S. John F. Kennedy was significantly overhauled in the 1990s to extend its life until 2013. Although the cost to operate the CV-67 would total about $300 million a year, CBO estimates that savings would be insignificant relative to the President's most recent budget proposal because the Navy has not requested sufficient funds in their future plans to operate the carrier over the 2007-2011 period.

Compensation and Benefits. S. 2766 contains several provisions that would affect compensation and benefits for uniformed personnel.

Pay Raises. Section 601 would raise basic pay for all individuals in the uniformed services by 2.2 percent, effective January 1, 2007. CBO estimates that implementing the 2.2 percent raise would cost about $1.3 billion in 2007. Because this pay raise is equal to the raise authorized under current law, there is no incremental cost for this provision. In addition, this section would extend the pay table to 40 years of service and would authorize additional raises targeted to warrant officers and senior enlisted personnel that would be effective on April 1, 2007. CBO estimates that the incremental costs associated with extending the pay table and the targeted raises would be about $196 million in 2007 and total $1.9 billion over the 2007-2011 period.

Expiring Bonuses and Allowances. Sections 611 through 614 would extend DoD's authority to pay certain bonuses and allowances to military personnel. Under current law, most of these authorities are scheduled to expire in December 2006, or three months into fiscal year 2007. The bill would extend these authorities for another year. Based on data provided by DoD, CBO estimates that the costs of these extensions would be as follows:

- Authorities to make special payments and give bonuses to certain health care professionals would cost $22 million in 2007 and $21 million in 2008;

- Special payments for aviators and personnel qualified to operate and maintain naval nuclear propulsion plants would cost $106 million in 2007 and $70 million in 2008;

- Retention and accession bonuses for officers and enlisted members with critical skills would cost $105 million in 2007 and $44 million in 2008;

- An extension of authorities for assignment incentive pay (which currently expires at the end of calendar year 2007) and for pay for reservists in high priority units would cost $19 million in 2007 and $55 million in 2008;

- Payment of reenlistment bonuses for active-duty and reserve personnel would cost $886 million in 2007 and $347 million in 2008; and

- Enlistment bonuses for active-duty and reserve personnel would cost $389 million in 2007 and $255 million in 2008.

Most of these changes would result in additional, smaller costs in subsequent years because many payments are made in installments. In total, extending authority for the expiring bonuses and allowances would cost about $1.5 billion in 2007 and $3.1 billion over five years.

Special Pay for Reserve Health Care Professionals. Section 615 would increase special pay for certain reserve health professionals from the current rate of $10,000 per year to a maximum rate of $25,000 per year. To qualify for the special pay, these health professionals must be reservists who are designated as part of a critically short wartime specialty and who agree to sign a one- to three-year enlistment contract. Based on information from DoD, CBO estimates that over 800 qualifying medical professionals will sign new enlistment contracts between October 1, 2006, and December 31, 2007 (this special pay would require reauthorization each calendar year). Assuming each of these servicemembers signs a three-year enlistment agreement and receives anniversary payments each year, CBO estimates the total cost of this section would be $10 million in 2007 and $37 million over the 2007-2010 period.

Accession Bonuses for Health Specialties. Section 616 would expand and enhance recruitment bonuses for dentists and for officers trained in critical health care specialties. CBO estimates that, taken together, these authorities, which would expire on December 31, 2007, would cost $19 million in 2007 and $24 million over the 2007-2008 period.

Section 616 would increase the maximum accession bonus for dental officers from $30,000 to $200,000. Based on information from the services, CBO expects the average bonus paid under this authority would increase to $100,000. Currently, about 60 dentists receive this bonus each year. Therefore, increasing the average bonus by $70,000 would cost $4 million in 2007 and $5 million over the 2007-2008 period.

In addition, section 616 would create new accession bonuses for both dentists and physicians in critically short wartime specialties. In both cases, the maximum amount of the bonus would be $400,000. Based on information from the services, CBO estimates that about 50 dentists and physicians would receive this bonus in the first year and that the average bonus would be about $300,000. Therefore, CBO estimates the cost of these new accession bonuses would be $15 million in 2007 and $19 million over the 2007-2008 period.

Voluntary Separation Pay. Section 618 would enhance authorities related to the payment of voluntary separation pay. The Navy and Air Force currently plan to reduce their force levels by tens of thousands of personnel over the next several years. To help achieve those goals, the National Defense Authorization Act for Fiscal Year 2006 (Public Law 109-163) authorized the services to use voluntary separation pay as an incentive to encourage officers with less than 12 years of service to leave the military. That authority will expire at the end of calendar year 2008. Section 618 would extend that authority through the end of calendar year 2012 (or the first quarter of fiscal year 2013), and expand it by increasing both the maximum payment and the eligible population (as opposed to the House-passed version of the National Defense Authorization Act for Fiscal Year 2007, which would only extend current authorities through calendar 2009 and expand the eligible population, but would not increase the maximum allowable payment). CBO estimates that the cost of implementing section 618 would be $132 million in 2007 and $2.0 billion over the 2007-2011 period.

Based on information from the services, CBO estimates that by extending the current authority to December 31, 2012, section 618 would allow the services to offer voluntary separation pay of almost $100,000 to an additional 6,100 officers. Thus, CBO estimates the cost of this extension would be $181 million in 2009 and $567 million over the 2009-2011 period.

Section 618 also would double the maximum allowable separation payment and eliminate the current restriction that voluntary separation pay be given only to officers with less than 12 years of service. The services indicate that both of these changes to the current authority would be used primarily to encourage officers with 12 or more years of service to leave the military. Based on information from the services, CBO estimates that about 3,500 additional personnel would receive payments under this expanded authority. Taking into account the change in the maximum payment formula, combined with the fact that the formula is dependent on rank and years of service, CBO estimates the average payment to these members would be about $400,000. Thus, the combined cost of eliminating the years-of-service restriction and changing the maximum allowable payment would be $132 million in 2007 and $1.4 billion over the 2007-2011 period, CBO estimates.

Health Professions Scholarship and Financial Assistance Programs. Section 564 would increase the stipends and grants paid to students enrolled in the Health Professions Scholarship and Financial Assistance Programs. The Health Professions Scholarship Program (HPSP) pays the tuition of students studying to become health professionals in return for an obligation to serve in the armed forces upon completion of their training. Along with tuition, students enrolled in the program receive a stipend to help defray living expenses while they are still attending school. Under current law, the stipend is limited to about $13,000 per year. Section 564 would increase the maximum stipend to $30,000. (Under both current law and the proposal the stipend is adjusted each year for inflation.) Because the services are having difficulty recruiting medical professionals, CBO believes DoD would increase the stipend to the maximum amount. Based on data from DoD, current plans are to enroll about 5,300 students in HPSP each year. This number also includes students in the Specialized Training Assistance Program, who are authorized by statute to receive the same stipend as those participating in HPSP. Therefore, CBO estimates an increase in the maximum stipend would cost $88 million in 2007 and $466 million over the 2007-2011 period.

In addition to the stipend, the Financial Assistance Program pays an annual grant of about $28,000 to students who are engaged in specialized medical training. Section 564 would increase the maximum amount of this grant to $45,000 per year. (Under both current law and the proposal the grant is adjusted each year for inflation.) According to data from DoD, current plans are to pay this grant to about 200 students each year. Assuming all of these students receive the maximum grant, the total cost to DoD would be $3 million in 2007 and $17 million over the 2007-2011 period. Including changes to both the stipend and the grant, CBO estimates the total cost of implementing section 564 would be $91 million in 2007 and $483 million over the 2007-2011 period.

Education Loan Repayment for Health Professionals. Section 563 would increase the amount of student loans DoD can repay on behalf of health professionals who enlist in the armed forces to a maximum of $60,000 for each year of obligated service. Based on information from DoD, CBO estimates about 600 health professionals would enlist in the armed forces each year using this enhanced benefit. However, about 250 of these personnel would be nurses, who, on average, have smaller student loans than physicians or dentists, and for whom the current annual repayment ceiling is generally sufficient. Of the remaining 350 physicians and dentists, CBO estimates the average amount of medical school debt for this group is about $131,000 per person, based on information from the Association of Medical Colleges and from DoD.

For fiscal year 2007, CBO estimates the maximum amount DoD can repay under current law will be about $32,500 for each year of service. Since the average service obligation is three years, DoD will only be able to repay about $100,000 of medical loans for each new member, which is $31,000 less than the average incurred debt. Increasing the maximum repayment amount to $60,000 for each year of service would allow DoD to repay the full amount of these medical school loans with the same years of obligated service. Thus, for a three-year enlistment, DoD would pay an extra $10,000 per year on average to repay loans for each new doctor or dentist. CBO estimates the cost of this section would be $4 million in 2007 and would increase each year as additional new enlistees take advantage of the higher loan repayment benefit so that the total cost would be $49 million over the 2007-2011 period.

Survivor Benefit Plan (SBP) Benefits. For certain survivors, section 642 would repeal the current reduction to SBP annuities by the amount of any Dependency and Indemnity Compensation (DIC) payments.

The military retirement system, which pays annuities to military retirees and their survivors, receives annual payments from appropriated funds based on an estimate of the system's accruing liabilities. If this provision is enacted, the yearly contribution to the Military Retirement Fund (an outlay in budget function 050, national defense) would increase to reflect the added liability from the expected increase in annuities to the survivors of future servicemembers and retirees. Using information from DoD, CBO estimates that implementing this provision would increase such payments by $23 million in 2007 and about $116 million over the 2007-2011 period. CBO estimates that enacting this provision also would increase direct spending for survivor benefits by about $659 million over the 2007-2016 period. Those mandatory costs are discussed below, in the "Direct Spending" section.

Other Provisions. In addition to the provisions discussed above, CBO estimates other provisions in the bill would increase both military and civilian compensation and benefits by $14 million in 2007 and $24 million over the 2007-2011 period:

- Section 534 would create a pilot program to reintegrate National Guard members into civilian life after deployments;
- Section 561 would allow commissioned officers to attend medical school;
- Section 604 would extend the prohibition against charging certain injured servicemembers for meals at military treatment facilities;

- Section 605 would authorize a second basic allowance for housing for unmarried reserve members activated as part of a contingency operation;

- Section 606 would allow the spouses of members that die on active duty to temporarily receive that member's housing allowance, even if the spouse is a member of a uniformed service;

- Section 617 would increase the maximum amount of the nuclear career accession bonus to $30,000;

- Section 618 would increase the incentive bonus for transfer between armed forces to $10,000; and

- Section 1103 would equalize benefits for civilian personnel on official duty in Iraq and Afghanistan.

Defense Health Program. Title VII contains a number of provisions that would affect DoD health care benefits, with the most significant provision prohibiting private-sector companies and state and local governments from encouraging their employees to use TRICARE instead of the employers' group health insurance plans.

Prohibition on Employers Encouraging Military Retirees to use TRICARE. Section 722 would prohibit employers from encouraging their employees to forgo enrollment in a group health plan and to use TRICARE instead. This ban would take effect on January 1, 2008. Currently, some private-sector companies and state and local governments are encouraging those employees who are also military retirees under age 65 to use TRICARE for health care coverage instead of the insurance plans sponsored by the employer. Most of those employers are offering to purchase a TRICARE supplemental policy for those employees and any eligible family members. Such supplemental insurance generally covers all deductibles, copayments, and other TRICARE cost-sharing amounts. These supplemental insurance policies cost as little as $60 per month for single coverage while it can cost employers more than $5,500 per year to provide full health insurance coverage for an employee. DoD reports that, in 2007, it will cost about $3,000 a person to provide health care under its TRICARE Standard program.

Based on data from DoD about the number of retirees under age 65 and their dependents under age 65 and data from surveys and studies about the percentage of retirees currently being offered incentives to forgo employer-sponsored insurance, CBO estimates that about 50,000 people a year are being diverted from employer-sponsored plans to TRICARE. Thus, under section 722, CBO estimates that 50,000 retirees and their dependents would stop using

TRICARE in favor of an employer-sponsored plan, for a savings to DoD of about $119 million in 2008 and $700 million over the 2008-2011 period.

TRICARE Pharmacy Copayments. Section 702 would eliminate copayments for prescriptions obtained through the TRICARE mail-order program (TMOP) and require that most refills of maintenance medications be filled through TMOP. Currently, TRICARE participants can choose to have prescriptions filled in one of three ways: through the TMOP, at military treatment facilities (MTFs), or at retail pharmacies. In 2007, beneficiaries will be charged copayments of $5 for generic drugs and $15 for brand-name drugs at retail pharmacies and $9 for brand-name drugs obtained through the TMOP. There would be no copayment for generic drugs obtained through the TMOP, nor for drugs obtained at MTFs. Those copayment amounts apply to active-duty dependents and all retirees and their dependents. Health care costs for active-duty dependents and retirees and dependents under age 65 are discretionary costs and are covered in this part of the estimate. Retirees and their dependents age 65 and older are covered under TRICARE For Life, which is classified in the budget as a mandatory (i.e., direct spending) program. CBO's evaluation of the pharmacy costs for that group of beneficiaries is discussed later in the "Direct Spending" section.

Based on data provided by DoD, CBO estimates that in 2007 almost 60 million prescriptions for a one-month supply of a drug will be filled through the three outlets for active-duty dependents and retirees and their dependents under age 65. Active-duty dependents have the vast majority of their prescriptions filled at MTFs. Retirees and their dependents under age 65 have about half of their prescriptions filled at MTFs and more than one-third filled at retail pharmacies. Based on analysis by DoD, CBO estimates that 65 percent of all prescriptions obtained at retail pharmacies and MTFs are refills of maintenance medications that will have to be filled through the TMOP beginning April 1, 2007. By eliminating TMOP copayments, CBO estimates that DoD collections would be reduced by about $34 million in 2007 and $349 million over the 2007-2011 period.

Transferring prescriptions from the other two outlets to the TMOP would also result in cost changes for DoD in addition to the changes in collections from the copayments. While it costs DoD about $20 to fill each generic prescription at MTFs, at retail pharmacies, and through the TMOP, the average cost for DoD to provide brand-name drugs varies, depending on the population and how the drug is dispensed. Though retirees and their dependents use more expensive drugs than do active-duty dependents, it is cheaper for DoD to fill the prescription for both groups through the TMOP than through a retail pharmacy and cheaper still to do it through an MTF, which dispenses the drugs directly to beneficiaries. Thus, the cost to DoD decreases when beneficiaries switch from retail pharmacies to the mail-order program but the cost increases when they switch from MTFs to mail order. CBO estimates that the savings from transferring prescriptions from retail pharmacies to the TMOP would be about $114 million in 2007 and $702 million over the 2007-2011 period. CBO estimates that the costs for transferring prescriptions from MTFs to the TMOP would be about $131 million in 2007 and $814 million over the 2007-2011 period.

In total, CBO estimates that implementing section 702 would increase discretionary costs by $49 million in 2007 and $459 million over the 2007-2011 period.

Establishment of Disease Management Programs. Section 728 would require DoD to establish disease and care management programs throughout the military health care system for six specific chronic diseases and conditions: diabetes, cancer, heart disease, asthma, chronic obstructive pulmonary disorder, and depression and anxiety disorders. In general, disease management programs attempt to identify beneficiaries at risk of developing a disease, ensure early screenings, educate patients about ways to prevent some diseases, and encourage useful treatment for those who do have the disease or condition. One purpose of these programs is to reduce long-term costs by spending more initially for preventative measures, though studies have shown that this is not always the outcome. Heart disease programs have been shown to reduce total costs over time, while programs for depression can have the opposite effect.

Based on information from DoD, CBO estimates that it would cost $10 million in the first year to establish the disease management programs and an additional cost of about $750 per participant to operate the programs. Based on information from DoD, CBO expects that, after the initial implementation costs, DoD would experience a 75 percent return on investment over a five-year period; that is, for every dollar spent per participant, DoD would eventually save 75 cents. Based upon the incidence rates of these six diseases and conditions in the general population, CBO estimates that less than 20 percent of the almost 6 million beneficiaries have one or more of these conditions. A smaller percentage would be targeted as potentially benefitting from a disease-management program. CBO also estimates that about one-half of the targeted population would participate in a disease-management program and that it would take about three years for the programs to provide care and assistance to all of those participants. Accounting for a small amount of DoD funding already dedicated to disease management, CBO estimates that implementing section 728 would increase net costs by $10 million in 2007 and about $250 million over the 2007-2011 period. Net costs of these programs could be either greater or lower than those amounts, depending on how successful they are in reducing long-term costs of the targeted diseases.

Enrollment in TRICARE Standard. Section 723 would require that DoD establish a system of enrollment for some beneficiaries of the TRICARE Standard program by October 1, 2007, and charge a fee for enrolling. It would also require that everyone who enrolls be provided an opportunity to have their health-related risks evaluated. CBO estimates that implementing this section would cost $20 million in 2007 and about $41 million over the 2007-2011 period.

TRICARE Standard is a health care program similar to most fee-for-service insurance plans, except that users do not have to enroll prior to making claims. Retirees and their dependents under age 65, who would be required to enroll under this provision, use TRICARE Standard in different ways. Some beneficiaries use the program as their primary health care plan. Others, who may have health insurance through a spouse or an employer, use it as a supplemental plan. Many of those who are eligible may not use TRICARE at all in any given year. Section 723 would require, before making a claim, that a beneficiary be enrolled in the program at a one-time cost of $25 for an individual and $40 for a family. In 2008, over 1 million retirees and dependents under age 65 (reflecting almost 450,000 individual and family plans) are expected to use TRICARE Standard. CBO expects that nearly all of those beneficiaries would enroll in order to continue receiving care and that there would be about 55,000 new enrollees each subsequent year. Given that 90 percent of beneficiaries are likely to enroll for family coverage, CBO estimates that DoD would collect enrollment fees of about $17 million in 2008 and $1 million per year thereafter.

Based on information from DoD, CBO expects that it would cost DoD about $17 million in 2007 to develop an enrollment system. In addition, there would be an administrative cost per beneficiary. Based on data provided by DoD, CBO estimates that it would cost about $28 million in 2008 and $1 million per year thereafter to administer the enrollment program.

Section 723 would also require that all beneficiaries, at the time of enrollment, be offered an opportunity to have an assessment made of their health-related risks. Based on information from DoD, CBO estimates that it would cost DoD about $3 million in 2007 to develop an approach to measure health risk. Not all beneficiaries would opt to take the assessment, but for those who would, CBO expects that some would receive a recommendation to see a physician and would make an appointment that would not otherwise have been made. Based on information provided by DoD, CBO estimates that the risk assessment would cause about 35,000 people to see a doctor in the first year and fewer than 2,000 every year after. With an average cost per visit of about $200, CBO estimates that this assessment would increase costs for doctor's visits by about $7 million in 2008 and by less than $500,000 each subsequent year.

Incentive Payments. Section 724 would make permanent a program to provide extra money to doctors who treat TRICARE beneficiaries in geographical areas with a shortage of primary care physicians. TRICARE has historically provided the same incentive payments as those found in the Medicare program. This incentive payment, which provides an extra 5 percent on top of the standard amount payable for care, is scheduled to expire at the end of this year.

Section 724 would mandate that the payment resume as of January 1, 2008. (The section also mandates an incentive payment to physicians in specialties in which there is a shortage of doctors, but this is already a permanent part of the TRICARE program.)

Based on the amounts currently paid to doctors in areas which have been identified as having a shortage of primary care physicians, CBO estimates that resuming this payment program would cost DoD $5 million in 2008 and $30 million over the 2008-2011 period.

Other Provisions. The bill contains various other provisions that would affect the cost of discretionary programs over the 2007-2011 period.

Telecommunications Benefit Program. Section 373 would expand and extend the DoD Telecommunications Benefit Program established in current law. Under this program, DoD provides up to $40 per month of phone and e-mail services to certain members of the armed forces who are stationed outside of the United States in direct support of Operation Enduring Freedom or Operation Iraqi Freedom. Section 373 would expand this to include other contingency operations that might arise and would eliminate the September 30, 2006, sunset date. In addition, section 373 would expand program eligibility to include servicemembers who are hospitalized because of wounds received in a contingency operation. Based upon information from DoD on the number of individuals who have qualified for the benefit previously and CBO assumptions about future troop levels in qualifying locations, CBO estimates that this provision would cost $64 million in 2007 and approximately $190 million over the 2007-2011 period.

Defense Acquisition Challenge Program. Section 802 would extend the authorization of the Defense Acquisition Challenge Program past its current expiration of September 30, 2007, to September 30, 2012. This program is responsible for reviewing and testing proposals to improve the performance of current DoD acquisition programs. Based upon information from DoD, CBO estimates that implementing this provision would cost $30 million in 2008 and $125 million over the 2008-2011 period.

Matters Relating to Other Nations. Section 1023 would increase, from $40 million to $80 million, the maximum amount authorized for counterdrug assistance in the years 2007 and 2008. It also would make an additional 15 countries eligible for that support. Section 1202 would authorize an additional $5 million to pay for foreign officials to attend training programs conducted under the Regional Defense Counterterrorism Fellowship Program ($20 million is currently authorized for that purpose). Based on information from DoD, CBO estimates that the department would use all available funds for these two programs.

Use of Armed Forces in Major Public Emergencies. Section 1042 would amend the Insurrection Act to make explicit the President's authority to deploy the armed forces, including the National Guard, within the United States to restore order or enforce federal law after a major public emergency, such as a natural disaster, epidemic, or terrorist attack. Current practice, in a major public emergency, is for the governor or legislature of a state to request assistance from the federal government. The Federal Emergency Management Agency then organizes the federal government's response to that request.

This provision would clarify the President's authority to deploy the armed forces in response to public emergencies without first receiving a request from state authorities in cases where the President determines such action is necessary to restore public order or enforce federal law. This section also would authorize the President to direct the Secretary of Defense to provide supplies, services, and equipment to persons affected by such an emergency. If this clarification would encourage the President to use the armed forces more frequently or more intensively than is the current practice, the potential cost could be significant. However, because CBO does not have a basis for determining the frequency of such emergencies or the magnitude of the potential involvement of the armed forces, CBO has no basis for predicting the potential cost of this section.

Direct Spending and Revenues

The bill contains provisions that would both increase and decrease direct spending, primarily by expanding DoD's ability to use third-party financing for the construction of military housing and through changes to survivor benefits and TRICARE. We estimate that those provisions combined would increase direct spending by about $1.4 billion over the 2007-2011 period and by $2.0 billion over the 2007-2016 period (see Table 4). S. 2766 also would decrease federal revenues by about $1 million over the 2007-2016 period.

Updating Foreign Currency Fluctuation Adjustment For Certain Military Family Housing Leases in Korea. DoD has authority under Title 10, United States Code, section 2828 to lease 2,800 family housing units in Korea, at a maximum cost of no more than $35,000 per unit. Under current law, that cost limit is adjusted for the change in the consumer price index since 2003, and for the change in the foreign currency exchange rate since 1988. Section 2809 would modify the adjustment for foreign currency fluctuations by changing the base year for that adjustment to 2003. The adjusted cost limit for leased housing in Korea is currently $30,367 per unit—less than the unadjusted cost limit of $35,000. That limit would increase to $47,522 using the method proposed in section 2809.

TABLE 4. ESTIMATED IMPACT OF S. 2766 ON DIRECT SPENDING AND REVENUES

	By Fiscal Year, in Millions of Dollars									
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
CHANGES IN DIRECT SPENDING										
Military Housing in Korea										
Estimated Budget Authority	160	160	160	0	0	0	0	0	0	0
Estimated Outlays	10	58	109	126	92	48	22	10	5	0
Pilot Projects for Military Housing										
Estimated Budget Authority	0	0	30	0	0	0	0	0	0	0
Estimated Outlays	0	0	4	14	9	2	1	0	0	0
Maximum Term of Leases for Overseas Facilities										
Estimated Budget Authority	1	2	5	5	5	5	5	5	5	5
Estimated Outlays	*	1	3	5	5	5	5	5	5	5
SBP Benefits										
Estimated Budget Authority	53	57	61	63	66	68	70	72	74	76
Estimated Outlays	53	57	61	63	66	68	70	72	74	76
Paid-Up SBP										
Estimated Budget Authority	202	213	0	0	0	0	0	0	0	0
Estimated Outlays	202	213	0	0	0	0	0	0	0	0
TRICARE Pharmacy Program										
Estimated Budget Authority	42	61	62	54	46	39	31	22	12	2
Estimated Outlays	42	61	62	54	46	39	31	22	12	2
Total Changes										
Estimated Budget Authority	458	493	318	122	117	112	106	99	91	83
Estimated Outlays	307	390	239	262	218	162	129	109	96	83
CHANGES IN REVENUES										
Thrift Savings Plan										
Estimated Revenues	*	*	*	*	*	*	*	*	*	*

NOTES: Numbers in the text may differ from figures shown here because of rounding.

SBP = Survivor Benefit Plan.

* = between -$500,000 and $500,000.

Based on information provided by DoD, CBO expects the department would use the increased authority to enter into build-to-lease housing contracts that are not financially viable under current law. In a build-to-lease agreement, the government contracts with a developer to build a specified number of housing units in a specified location for use by military personnel. According to DoD, the military services often agree to a fixed lease term—currently limited to a maximum of 15 years in Korea—with renewal options for additional periods of time. Those renewal options can extend the duration of the lease term to 30 years or more. Based on the government's commitment to lease the housing, the developer borrows money to pay for construction of the units, using the promised payments from the government to demonstrate to lenders a reliable source of income for debt service.

CBO believes that acquiring military housing through a build-to-lease contract is a governmental activity that uses a private-sector intermediary to serve as an instrument of the federal government by borrowing funds to finance the construction of housing on the government's behalf. Those build-to-lease agreements should be considered acquisitions—rather than leases—for several reasons. First, the housing would be constructed at the request of the government to fill an enduring need for housing for DoD personnel. Second, because the government would agree to lease the housing for up to 15 years, and may extend the lease term for additional years under renewal options, the government would likely consume most of the useful economic life of the housing. Third, the need for at least 15 years of government commitment to obtain financing indicates that there may not be a private-sector market for the new housing. Finally, the government would be the dominant or only source of income for such projects. Lease payments are made directly by the government to the housing developer. If the lease is terminated before the end of the fixed term, or before the end of any exercised lease options, the government is liable for early termination costs, which, under DoD's current practice, are not funded in the budget when the lease is signed. The federal government also agrees to pay rent on all the units it leases, regardless of whether they are occupied by DoD personnel or are vacant.

DoD requested the increase in the cost limit for leases adjusted for inflation and foreign currency fluctuation because it has an enduring need for housing in Korea that cannot be satisfied under the limits on the authority provided in current law. According to DoD, the lease payments under the current cost limit calculation do not provide enough income for housing developers in Korea to recover their construction costs during the 15-year term of the lease. Increasing the cost limit would allow DoD to pay developers more during the guaranteed term of the lease, making those projects financially viable.

The acquisition cost of the housing that would be acquired using this increased authority is determined by calculating the present value of 15 years of lease payments less the portion of those payments needed for operating and maintenance costs. (On average, such operating and maintenance costs account for about $18,000 per unit each year.) That amount should be recorded as budget authority in the year the lease is signed, and outlays should be recorded over the construction period. CBO estimates that under the cost limit for those leases in current law, the maximum acquisition cost of housing that could be acquired is approximately $125,000 per unit. Raising the cost limit for those leases by adjusting for foreign currency fluctuations from 2003 rather than 1988 would increase that maximum acquisition cost to approximately $300,000 per unit. This legislation would increase spending in the amount of the difference of the maximum acquisition cost under current law, and that acquisition cost as adjusted by section 2809.

DoD has indicated it would use the expanded leasing authority to acquire 2,800 family housing units for military personnel in Korea, without having appropriations for the full cost of that housing when the agreement to lease the housing is signed. CBO assumes that those units would be acquired over the 2007-2009 period, and estimates that enacting this modification would increase direct spending by $10 million in 2007, $395 million over the 2007-2011 period, and $480 million over the 2007-2016 period.

Pilot Projects for Acquisition or Construction of Military Unaccompanied Housing. Section 2810 would expand the Navy's authority to use third-party financing to acquire housing for unaccompanied military personnel by extending the expiration of that authority from September 30, 2007, to September 30, 2009.

Currently, DoD is authorized to use direct loans, loan guarantees, long-term outleases, rental guarantees, barter, direct government investment, and other financial arrangements to renovate, build, and operate military housing in concert with housing developers. DoD typically enters into a series of long-term agreements with a developer who establishes a limited liability company (LLC) or other special-purpose entity, specifically for the purpose of renovating, constructing, operating, and maintaining the military housing at the project. DoD contributes some combination of land, existing housing, and cash to the partnership or LLC. On behalf of the government, the LLC then borrows additional money for the project from a third party, such as a commercial mortgage corporation, to finance construction. In other words, the third-party financier acts as an intermediary by borrowing money—instead of the U.S. Treasury—to finance a governmental activity. The value of the assets contributed by the government serve as collateral for the borrowing and the future rent payments (over a period of 30 to 50 years) from military personnel provide a reliable source of income for debt service.

CBO believes that acquiring housing for military personnel in that manner is a governmental activity that uses a private-sector financial intermediary to serve as an instrument of the federal government. In CBO's view, ventures that borrow funds to construct or refurbish military housing should be treated as governmental and their investments should be recorded up front, as borrowing authority—a form of budget authority. Amounts expended by these public-private ventures should be recorded in the budget as outlays at the time they occur.

Title 10, United States Code, section 2881a provides authority for the Navy to pursue three pilot projects to acquire housing for unaccompanied sailors. Under that authority, the Navy can make rental payments directly to the housing developer in excess of the partial basic allowance for housing paid to personnel living in government quarters. Based on information from the Navy, CBO estimates that only two housing projects will be acquired before the current expiration date of September 30, 2007. CBO estimates that extending the deadline until the end of fiscal year 2009 would allow the Navy to acquire one more housing project than it could acquire under current law. CBO estimates that the Navy would acquire that additional project in 2009.

Based on information from the Navy, CBO estimates that this additional construction activity would have no cost in 2007 or 2008, but would increase outlays by $27 million over the 2009-2011 period and by $30 million over the 2009-2016 period.

Extending the Maximum Lease Term for Overseas Facilities. DoD is authorized to lease overseas facilities other than family housing units for a maximum term of five years. Section 2826 would extend that maximum lease term to 10 years.

According to information provided by DoD, the facilities that it leases overseas usually require costly modifications to meet government requirements. The lessor amortizes the cost of those modifications over the term of the lease. Because DoD becomes obligated to pay the full cost of those modifications when it enters those leases, the costs should be recorded in the budget in the year the lease is signed, rather than amortized over the lease term. The Office of Management and Budget permits DoD to incur those obligations if it has appropriations sufficient to cover the cost of the lease in the first year, thus allowing the department to incur that obligation in advance of appropriations. CBO believes that this practice is inconsistent with governmentwide accounting principles.

Because DoD could spread the cost of the initial modifications over a larger number of years, extending the maximum lease period would result in smaller annual lease payments. Therefore, CBO expects that DoD would enter into more leases if the maximum lease term was increased from five to 10 years. Because the department would be able to sign lease contracts and incur the additional obligations without having an appropriation for the full amount of that obligation, this bill would provide contract authority—a form of budget authority. CBO estimates that such spending on overseas leases will not increase significantly in 2007 but would cost $14 million over the 2007-2011 period and $39 million over the 2007-2016 period.

Survivor Benefit Plan Benefits. Under current law, survivors of members of the uniformed services are eligible for a survivor annuity if the servicemember died on active duty or, upon retirement, enrolled in SBP and made monthly premium payments. Survivors who receive both SBP annuities and Dependency and Indemnity Compensation (a benefit paid by the Department of Veterans Affairs to the survivors of servicemembers who died on active duty and the survivors of veterans who died of a service-connected disability) see their SBP annuities reduced by the amount of any DIC payment. (Those affected are entitled to refunds of any premiums paid for the unpaid portion of the SBP annuity.)

Section 642 would eliminate this reduction for two specific groups of annuitants: survivors of those who died on active duty (in the line of duty), and survivors of reservists who either were eligible for SBP but had not yet decided to participate (but were still within 90 days of receiving notification of eligibility for retirement) or who died during training while in an "inactive" status. CBO estimates that enacting this section would result in additional direct spending for survivor annuities of $53 million in 2007, $300 million over the 2007-2011 period, and $659 million over the 2007-2016 period. CBO estimates that there also would be discretionary costs of $116 million over the 2007-2011 period associated with this provision. These discretionary costs were discussed earlier in the "Spending Subject to Appropriation" section.

(If section 642 were written so as to repeal the offset for all annuitants, the cost would be significantly higher. CBO estimates that fully repealing DIC offsets of SBP for all annuitants would cost $4.4 billion over the 2007-2011 period, and $9.6 billion over 10 years. Further, the discretionary costs would increase from $116 million over five years to nearly $1.7 billion over the same period.)

Paid-Up SBP. Under current law, military retirees who are both 70 years of age and have paid SBP premiums for at least 30 years will be allowed to cease making such payments as of October 1, 2008. Section 643 would advance the effective date for that change by two years, to October 1, 2006. Since SBP premiums are deducted from retirees' annuities, eliminating those payments for certain retirees would increase outlays for retirement annuities. Based on information from DoD, CBO estimates that enacting section 643 would increase direct spending for retirement annuities by $202 million in 2007, and $415 million over both the 2007-2011 and 2007-2016 periods.

TRICARE Pharmacy Copayments. Section 702 would eliminate copayments for prescriptions obtained through the TRICARE mail-order program and would require that most refills of maintenance medications be filled through TMOP. Retirees age 65 and older and their dependents age 65 and older are covered under TRICARE For Life, which is classified in the budget as a mandatory (i.e., direct spending) program. Health care costs for active-duty dependents and for retirees and dependents under age 65 are discretionary costs. CBO's estimate of the change in pharmacy costs under section 702 for that group of beneficiaries, along with a more-detailed description and analysis of the proposed changes to the program, is discussed in the "Spending Subject to Appropriation" section.

CBO estimates that the budget impact of eliminating brand-name drug copayments for TRICARE For Life beneficiaries filling prescriptions through the TMOP would be an increase in direct spending of $51 million in 2007, $372 million over the 2007-2011 period, and $567 million over the 2007-2016 period.

Transferring prescriptions to TMOP also would result in cost changes for DoD because it is cheaper to fill prescriptions through the TMOP than through retail pharmacies, but more expensive to fill prescriptions through the TMOP than through military treatment facilities, which dispense the drugs directly to the beneficiaries. CBO estimates that the savings from transferring prescriptions from retail pharmacies to the TMOP would be about $54 million in 2007, $593 million over the 2007-2011 period, and $1.5 billion over the 2007-2016 period. In contrast, CBO estimates that the costs for transferring prescriptions from MTFs to the TMOP would be about $44 million in 2007, $485 million over the 2007-2011 period, and $1.3 billion over the 2007-2016 period.

On balance, CBO estimates that implementing section 702 would increase direct spending by about $42 million in 2007, $265 million over the 2007-2011 period, and $371 million over the 2007-2016 period.

Retirement Accrual Payments. Section 641 would reduce the amount DoD must contribute to the Military Retirement Fund on behalf of activated reserve members. Under current law, DoD must contribute to the fund an amount equal to a percentage of servicemembers' basic pay. The contribution rates are based on an estimate of the accruing liability for retirement benefits. For fiscal year 2007, DoD estimates the contribution rates will be 26.4 percent for full-time, active-duty servicemembers and 16.7 percent for part-time reservists. The contribution rate for part-time reserve members is lower because they must wait until age 60 before they can receive payments from the fund, and thus will, in general, receive a less costly retirement package. Under DoD's interpretation of current law, the services must contribute to the retirement fund at the higher full-time rate for reservists called to active duty. Section 641 would change this policy by allowing DoD to make contributions for these reservists at the lower part-time rate.

Payments to the retirement fund are made from discretionary appropriations, and shown as intragovernmental transfers, with discretionary outlays shown against the military personnel accounts and offsetting receipts credited to the military retirement fund. Therefore, any reduction in contributions to the retirement fund would result in a loss of offsetting receipts. Under section 641, CBO estimates this loss of receipts would be in the hundreds of millions of dollars each year. However, because the amendments made by section 641 would not take effect until the start of fiscal year 2008, any loss of receipts would be contingent upon the enactment of future appropriations and, therefore, would not be considered direct spending.

Other Provisions. The following provisions would have an insignificant budgetary impact on direct spending:

- Section 371 would allow the Secretary of the Army to establish a program to sell demilitarized and recycled munitions and retain the proceeds to fund the reclamation, recycling, and reuse of conventional military munitions. CBO estimates that implementing this provision would have an insignificant net effect on direct spending because it would allow DoD to spend any receipts generated under this program.

- Section 507 would allow chief warrant officers who have failed to be selected for promotion twice to be allowed to continue on active duty at the discretion of the service secretaries. Under current law, formal selection boards must be convened to allow those servicemembers to remain on active duty. Thus, this section could reduce the number of annual retirements, thereby reducing retirement outlays. Based on information from the Department of Defense, however, CBO expects that very few officers would postpone their retirements because of this provision.

- Section 872 would extend by one year DoD's authority to settle financial accounts from contracts that were executed prior to September 30, 1996, and that have unreconciled balances of less than $100,000.

- Section 912 would extend a pilot program that allows DoD to provide satellite tracking services to non-U.S. government entities. Under this program DoD is allowed to charge fees to cover the cost of providing such services. CBO estimates that implementing this provision would have an insignificant net effect on direct spending because it would allow DoD to spend any fees it collects.

- Section 1051 would allow DoD to collect fees from individuals attending DoD conferences in amounts necessary to offset the cost of conducting such conferences. CBO estimates that implementing this provision would have an insignificant net effect on direct spending because it would allow DoD to spend fees collected to defray such costs.

- Section 3112 would allow the Secretary of Energy to enter into agreements with a foreign government, international organization, or any person to contribute funds for purposes of the Global Threat Reduction Initiative of the National Nuclear Security Administration. This section would allow the Department of Energy to retain those contributions and to use those amounts for purposes of the initiative. This authority would expire on December 31, 2013. Although we cannot estimate the time lag between receiving the contribution and spending it, CBO expects that the net effect of any such collections and expenditures would be insignificant.

- Section 3113 would allow the Secretary of Energy to enter into agreements with a foreign government, international organization, or any person to contribute funds for purposes of the Second Line of Defense program of the National Nuclear Security Administration. The section would allow DOE to retain the contributions and to use the amounts for purposes of the initiative. This authority would expire on December 31, 2013. Although we cannot estimate the time lag between receiving the contribution and spending it, CBO expects that the net effect of any such collections and expenditures would be insignificant.

Revenues

Current law requires the Secretary of the Army to initiate a pilot program in fiscal year 2006 offering matching contributions to the Thrift Savings Plan (TSP). The pilot program began in April 2006 and ends on September 30, 2006. The program is available to all new Army enlistees who elect to serve five or more years on active duty in critical specialities. Except for this pilot program, the armed forces cannot make matching contributions for first-time enlistees under current law.

Section 619 would extend the pilot program through December 31, 2008, to allow more opportunity for evaluation of the effectiveness of the policy. CBO expects that providing matching contributions encourages new enlistees to increase their participation in the TSP. Because income taxes are deferred on TSP contributions, the anticipated increase in contributions initially results in lower income-tax revenue. Additionally, the earnings would be taxable if the savings were invested in taxable accounts. Thus, the lack of taxation on the earnings reduces income-tax revenue.

For this estimate, CBO assumes that, under the pilot program, the Army would offer the opportunity to obtain matching contributions to approximately 5,000 first-time enlistees per year or about 6.5 percent of the enlistees expected through December 31, 2008. Because the size of the pilot program would be small, CBO estimates that the revenue losses would be less than $500,000 a year. The projected revenue loss of the pilot program would be about $1 million over the 2007-2016 period.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

Section 4 of the Unfunded Mandates Reform Act excludes from the application of that act any legislative provisions that enforce the constitutional rights of individuals. CBO has determined that section 1042 would fall within that exclusion because it would expand the authority of the President to employ the armed services to protect individuals' civil rights. Therefore, CBO has not reviewed that section of the bill for mandates.

Other sections of S. 2766 contain intergovernmental mandates as defined in the Unfunded Mandates Reform Act. It would prohibit employers and other providers of group health coverage from offering incentives to military retirees and their dependents to decline enrollment in the group health plan in favor of relying on TRICARE as the primary source of health coverage. That prohibition would be an intergovernmental mandate as defined in UMRA. CBO estimates that the costs of that mandate would likely fall below the threshold for intergovernmental mandates ($64 million in 2006, adjusted annually for inflation).

Prohibiting Providers of Group Health Plans from Offering Certain Incentives

Section 722 would prohibit employers and other providers of group health coverage from offering incentives to military retirees and their dependents to decline enrollment in the group health plan in favor of relying on TRICARE as the primary source of health coverage. That prohibition would be an intergovernmental mandate as defined in UMRA. Under current law, a number of state governments offer insurance policies that supplement TRICARE to employees who have retired from the military or dependents of military retirees who are eligible for TRICARE. In doing so, those employers realize savings because the costs of providing supplemental coverage is considerably less expensive than that of comprehensive, primary insurance.

If employers are prohibited from offering such supplemental policies or other incentives, the cost of providing health insurance to their employees would increase. Data for estimating the magnitude of such costs is limited, and estimates are particularly sensitive to changes in assumptions—for example, the number of employees who would have declined employer-sponsored insurance even in the absence of any incentive or estimates of how many employers offer such incentives. CBO estimates, however, that the mandate would likely impose costs on state, local, and tribal governments totaling between $35 million and $45 million annually.

Providing Benefits to State and Local Governments

This bill contains several provisions that would benefit state and local governments. Some of those provisions would authorize aid for certain local schools with dependents of defense personnel and convey certain parcels of land to state and local governments. Any costs to those governments would be incurred voluntarily as a condition of receiving federal assistance.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

Section 722 of the bill would prohibit employers and other providers of group health coverage from offering any financial or other benefit to employees eligible for TRICARE to decline enrollment in the group health plan in favor of relying on TRICARE as the primary source of health coverage. That prohibition would be a private-sector mandate as defined in UMRA. Under current law, some employers offer insurance policies that supplement TRICARE to employees who are eligible for TRICARE, most of whom are military retirees and their dependents and survivors. In doing so, those employers realize savings because the costs of providing supplemental coverage is considerably less expensive than that of comprehensive, primary insurance.

If employers were prohibited from offering such supplemental policies or other incentives, the cost of providing health insurance to their employees would increase. Data for estimating the magnitude of such costs are limited, and estimates are particularly sensitive to changes in assumptions—for example, the number of employees who would have declined employer-sponsored insurance even in the absence of any incentive or estimates of how many employers offer such incentives. CBO estimates, however, that the mandate would likely impose costs on private employers totaling $132 million annually. This amount would be slightly higher than the threshold for private-sector mandates ($128 million in 2006, adjusted annually for inflation).

PREVIOUS CBO COST ESTIMATE

On May 9, 2006, CBO transmitted a cost estimate for H.R. 5122, the National Defense Authorization Act for Fiscal Year 2007, as reported by the House Committee on Armed

Services on May 5, 2006. Differences in the estimated costs of S. 2766 and H.R. 5122 reflect differences in the two versions of the legislation.

In total, S. 2766 would authorize appropriations for 2007 of about $509 billion, or about $3 billion more than the $506 billion that would be authorized by H.R. 5122. Both of those totals include $50 billion for continued operations in Iraq and Afghanistan. Both S. 2766 and H.R. 5122 contain provisions that would affect direct spending, but the effects of the new direct spending under H.R. 5122 would be offset over the 2007-2016 period by the effects of additional asset sales authorized in that legislation.

Section 722 of S. 2766 would prohibit employers from encouraging their employees to use TRICARE instead of an employer-sponsored group health plan. This prohibition is very similar to one found in section 710 of H.R. 5122, the House version of the National Defense Authorization Act for Fiscal Year 2007. Because of updated information, CBO has changed its estimate of this provision to show smaller savings.

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